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April 27, 1999

Ms. Magalie Roman Salas
Secretary
Federal Communications Commission
The Portals
445 Twelfth Street, S.W.
TW-A325
Washington, D.C. 20554

Re: Inter-Carrier Compensation for ISP-Bound Traffic Reply Comments of the Association for Local Telecommunications Services in CC Docket No. 99-68

Dear Ms. Salas:

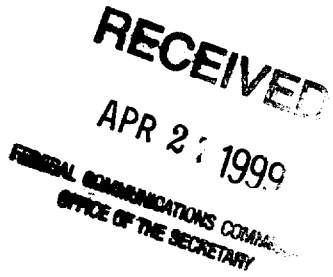
Enclosed please find an original and four copies of the reply comments of the Association for Local Telecommunications Services, as well as a disk containing an electronic version of the reply comments in the above-referenced proceeding. A disk copy is also being filed with ITS.

Sincerely,

Thomas Jones

Enclosures

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554



In the Matter of	)	
	)	CC Docket No 99-68
Inter-Carrier Compensation	)	
for ISP-Bound Traffic	)	

REPLY COMMENTS OF THE ASSOCIATION FOR LOCAL TELECOMMUNICATIONS SERVICES

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REPLY COMMENTS OF THE ASSOCIATION FOR LOCAL TELECOMMUNICATIONS SERVICES

I. INTRODUCTION AND SUMMARY

In determining the appropriate inter-carrier compensation for ISP-bound traffic on a going forward basis, the Commission must ensure that all inter-carrier compensation rules and rates are fair, reasonable, nondiscriminatory and conducive to creating market conditions that, at the very least, do not discourage entry. The Commission also must ensure that there is even-handed, non-discriminatory treatment of all carriers, consistent application of rate methodologies in all situations, and incentives for all carriers to accurately base their charges and compensation on the costs that they incur.

The ILECs' comments in this proceeding have generally challenged both the Commission's procedural and substantive tentative conclusions in the Notice of Proposed Rulemaking. The ILECs argue that the Commission should not and cannot, legally, require carriers to negotiate inter-carrier agreements covering ISP-bound traffic under Section 252 of the Communications Act of 1934, as amended by the Telecommunications Act of 1996 (the "Act"),

even when the Commission has established strong rules and principles that will limit and put boundaries around those negotiations and possible arbitrations. Nothing in the Act, however, so limits the Commission's or the states' authority. As long as there are strong federal rules that put the parties on notice as to what the rules and rates will be absent a voluntary negotiation covering these issues, negotiations and arbitrations within the context of Sections 251 and 252 are a reasonable and legal method of ensuring fair, reasonable and nondiscriminatory compensation.

Many of the ILECs also argue that "meet point billing" or other similar proposals that in essence are either bill and keep arrangements or some sort of revenue sharing are the appropriate inter-carrier compensation practice for ISP-bound traffic. These proposals, however, disregard the costs that any terminating LEC incurs in transporting and terminating this traffic and the significant costs that the originating LEC saves by not having to transport and terminate such traffic. In addition, there are a number of reasons why meet point billing is not an appropriate analog for this traffic. Meet point billing does not consider the significant switching costs that the terminating LEC incurs in delivering traffic to the ISP. Furthermore, there is absolutely no indication that the various "revenue sharing" or "division of revenue" proposals have any relationship to the cost incurred by the terminating LEC in transporting this traffic. As is more fully explained below, the ILECs' arguments that they are not recouping their costs in originating calls bound for ISPs are, at best, misleading. In any event, as indicated in ALTS's initial comments, if the ILECs are not recouping their costs, their remedy is with the state PUCs. The CLECs should not be made to bear the brunt of any alleged shortfall to the ILECs.

The Commission should adopt rules that govern state arbitrations of disputes concerning the exchange of ISP-bound traffic. These rules should ensure that the rates paid by all carriers are

reciprocal and based on a reasonable approximation of the additional costs incurred by the carriers. In addition, the Commission should require that the rules governing rates for local traffic subject to 251(b)(5) should apply to the exchange of ISP-bound traffic. The states have already established rates for 251(b)(5) traffic and, because the functionalities provided by CLECs in terminating both types of traffic are the same, the rates should be the same. Finally, the Commission should affirm that Section 252(i) rights apply to inter-carrier agreements relating to ISP-bound traffic.

II. THE COMMISSION HAS THE AUTHORITY TO ADDRESS THE INTER-CARRIER COMPENSATION ARRANGEMENTS THROUGH STATE SUPERVISED NEGOTIATIONS AND ARBITRATIONS PURSUANT TO STRONG FEDERAL RULES.

The ILECs argue that the FCC cannot require them to negotiate inter-carrier compensation for ISP-bound traffic pursuant to Sections 251-252 because neither Section 251(b) nor Section 251(c) requires such compensation.[1] A number of ILECs also argue that, for the same reason, the Act does not empower state commissions to impose inter-carrier compensation obligations on ISP-bound traffic within the context of a Section 252 arbitration.[2] Finally, Ameritech contends that, even if the FCC had the authority to direct state commissions to establish compensation arrangements for ISP-bound traffic, state commissions would nonetheless

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1 See, e.g., Ameritech Comments at 17-18; BellSouth Comments at 4-5; U S West Comments at 12-15.

2 See, e.g., Ameritech Comments at 18-19; GTE Comments at 12-14.

be precluded from exercising that power because they lack authority to regulate interstate traffic under state law.[3]

Contrary to the ILECs' claims, legal precedent and the plain language of Section 252 make it clear that the Commission has the authority to leave inter-carrier compensation for ISP-bound traffic to the states subject to federal guidelines. Similarly, if the FCC were instead to allow individual states to regulate inter-carrier compensation without federal guidelines, Sections 251(d)(3) and 261(c) of the Act provide a federal law basis for state commissions to exercise that authority.[4] Finally, Ameritech's argument that the state commissions would nonetheless lack authority to act under state law is a red herring. The question is not whether the states can act to regulate interstate traffic, but whether they can act to regulate inseverable, jurisdictionally mixed traffic in the absence of FCC preemption. A long line of federal case law interpreting Section 2(b) of the Act answers this question affirmatively.

A. FCC Authority

The ILECs erroneously argue that Sections 251-252 do not address inter-carrier compensation, and that, as a result, the FCC cannot delegate jurisdiction over such compensation to the states. This argument ignores circuit court precedent, reads non-existent limitations into Section 252, and, taken to its extreme, turns the logic underlying the Act on its head.

The Eighth Circuit has upheld the FCC's authority to allow state regulators to set rates for the recovery of interstate costs related to ISP-bound traffic in response to virtually identical

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3 See Ameritech Comments at 15-17.

arguments by many of the same parties. See Southwestern Bell Tel. v. FCC, 153 F.3d 523, 541-43 (8th Cir. 1998). In appealing the FCC's Access Charge Reform Order, petitioner incumbents challenged the FCC's authority to continue its practice of allowing ISPs to purchase business lines from intrastate tariffs as end users. Id. at 541-42. Incumbent petitioners claimed that the Commission's decision prevents them from recovering "undeniably interstate costs" not collected under the intrastate tariff, "amounts to a dereliction of the Commission's obligation to retain exclusive jurisdiction over interstate communications, and forces state regulatory commissions to overstep their authority by recovering interstate costs." Id. at 542.

The Eighth Circuit rejected the petitioners' arguments. The court observed that the FCC had determined that ISP services were jurisdictionally mixed and that it could not reliably separate the interstate and intrastate components. Id. at 543. Accordingly, the court upheld the FCC's discretion to require ISPs to pay intrastate charges for their business lines, while precluding assessment of access charges on ISP traffic. Id.[5] In so doing, the court affirmed the FCC's authority to share with the states rate-setting authority over charges relating to ISP-bound traffic, whether those charges relate to the rates paid by the ISP end users, as in the Southwestern Bell case, or to the rates paid by carriers to each other, at issue here. It follows therefore that, absent

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[4] Most ILECs concede that carriers are free to negotiate interconnection agreement terms that include inter-carrier compensation for ISP-bound traffic. See, e.g., GTE Comments at 13.

[5] Indeed, if anything, the Eighth Circuit was concerned that the FCC might be stepping on the states' toes by determining intrastate rates in contravention of the then-existing Iowa Utilities Board decision. See Southwestern Bell Tel., 153 F.3d at 543 ("nor can we conclude that [the FCC] has directed the States to inflate intrastate tariffs to cover otherwise unrecoverable interstate costs, thereby exceeding [FCC] authority").

an express prohibition, not present here, the FCC has the authority to share with the states its rate-setting powers.

Far from prohibiting such an arrangement, Section 252 of the Act affirmatively grants to the FCC the authority to allow states to set rates for inter-carrier compensation subject to federal guidelines. Section 252(b) provides that "the carrier or any other party to the negotiation may petition a State commission to arbitrate any open issues." The incumbents argue that they are only required to negotiate obligations enumerated in Sections 251(b) and (c); thus, "any open issue" must be limited to those duties. But Section 252(b) does not say "any open issue pursuant to the standards set forth in Section 251(b) or (c)." As demonstrated by the ILECs' own comments, where Congress intended to limit a requirement to an ILEC's duties under those sections, it certainly knew how to do so.[6]

Nor is it true, as GTE contends, that to read Section 252 to encompass issues not enumerated in Section 251(b) or (c) would conflict with Section 252(e)(2)'s requirement that an arbitrated agreement may only be rejected if it does not comply with Section 251, the Commission's regulations, or Section 252(d). GTE Comments at 13. GTE's argument ignores the language and structure of Section 252 of the Act and must be rejected.

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[6] Where a phrase is used in another part of the statute but omitted elsewhere, it can be assumed that the omission was deliberate. Cf. Cabell Huntington Hosp. v. Shalala, 101 F.3d 984, 988 (4th Cir. 1996) (use of different language in proximate subsection must be given effect by court when interpreting ambiguous statute); Rhode Island v. Narragansett Indian Tribe, 19 F.3d 685, 697-98 (1st Cir.), cert. denied, 115 S. Ct. 298 (1994) (when interpreting statute, first inquiry is whether statute is clear on its face; if so, there is no need to perform additional analysis).

Section 252 articulates a four-step process involving: (1) negotiation or mediation between the parties; (2) arbitration pursuant to Sections 252(b) and (c); (3) submission of an executed agreement to the commission for approval under Section 252(e); and (4) district court review, if necessary.[7] As noted, once the parties have negotiated for at least 135 days, either party may ask the state commission to arbitrate any open issues. An arbitrator reviews the parties' submissions, conducts a hearing, and ultimately issues an arbitration order ruling on "any open issues."[8] The arbitrator's order must comply with Section 252(c)'s standards, which requires ensuring that the agreement (1) meets the requirements of Section 251, including the FCC's regulations, (2) establishes rates pursuant to Section 252(d), and (3) provides an implementation schedule. The arbitrator's order directs the parties to incorporate terms reflecting its rulings, sometimes even recommending model language. Once the parties incorporate the arbitrator's rulings into their agreement, they submit the agreement, which has been "adopted by arbitration," to the state commission for approval pursuant to Sections 252(e)(1) and (e)(2)(B). It is at this point, and not before, that the state commission is bound by Section 252(e)(2)'s standard for rejecting "an agreement (or any portion thereof) adopted by arbitration under subsection (b)."

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7 See Michigan Bell Tel. v. MFS Intelenet, 16 F. Supp. 2d 817, 821 (W.D. Mich. 1998).

8 While the ILECs initially attempted to immediately appeal these orders, the district courts universally found such appeals premature. GTE Southwest, Inc. v. Graves, 989 F. Supp. 1148, 1150-51 (W.D. Okla. 1997); GTE Northwest, Inc. v. Nelson, 969 F. Supp. 654, 656 (W.D. Wash. 1997); GTE S., Inc. v. Morrison, 957 F. Supp. 800, 804 (E.D. Va. 1997).

The fact that the processes of adopting an agreement by arbitration and approval of an arbitrated agreement are sequential and governed by different standards is further demonstrated by a comparison of Section 252(c)'s arbitration standards to Section 252(e)(2)'s approval standards. First, Section 252(c) contains no language suggesting that it encompasses the entire universe of actions that an arbitrator may take during an arbitration. To the contrary, Congress's explicit limitation of the bases upon which a state commission may reject an agreement under Section 252(e)(2), when compared with Section 252(c)'s list of issues that must be addressed during an arbitration, underscores the lack of such exclusivity. Thus, Section 252(c) constitutes the minimum steps that a state commission must take in arbitrating an agreement; it in no way limits the arbitrator's authority to address other issues outside of an ILEC's enumerated duties under Sections 251(b) and (c).

Second, as noted, Sections 252(b)-(c) require the arbitrator to resolve open issues and impose conditions necessary to ensure compliance with Sections 251 and 252(d) (including FCC regulations) and to provide an implementation schedule. At the same time, Section 252(e)(2)(B) provides that the state commission, in reviewing an arbitrated agreement, can only reject that agreement if it fails to comply with Sections 251 or 252(d) (again, including FCC regulations). Notably, Section 252(e)(2)(B) does not allow the state commission to reject an agreement that lacks an implementation schedule. Yet Section 252(c) requires such a schedule. In addition to rendering Section 252(c)'s implementation schedule requirement superfluous, GTE's interpretation leads to an illogical result. According to GTE, Section 252(c) would mandate that the arbitrator require inclusion of an implementation schedule, while Section 252(e)(2) would preclude the commission from requiring inclusion of that schedule. GTE's construction is

therefore unsustainable. The Commission must exercise its authority to interpret the ambiguous provisions of Section 252 in a manner that is reasonable and internally consistent. The most reasonable interpretation is one that preserves the four-step structure of the Act, including the ability of the arbitrator to resolve any open issues (not just those enumerated in Section 251(b) and (c)) prior to an arbitrated agreement being submitted to the state commission for approval.

Analysis of the interaction between Section 252's arbitration and approval process and the Act's preservation of consistent state regulations also highlights a logical flaw in the ILECs' arguments regarding federal and state authority under Sections 251-252. If the FCC were to leave the regulation of ISP-bound traffic entirely to the states, without promulgating binding guidelines, Sections 251(d)(3) and 261(c) would permit the states to regulate inter-carrier compensation for the exchange of ISP traffic.[9] If the Commission were to accept the ILECs' arguments that the FCC cannot prescribe and enforce federal regulations within the context of interconnection agreements unless related to Section 251(b) or (c),[10] it would lead to the anomalous result that the states could require ILECs to incorporate terms into their agreements regarding intrastate services that are not enumerated in Section 251(b) or (c), yet the FCC could

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9 Ameritech is correct that federal authority is insufficient on its own. The regulatory commission must also possess state authority to exercise such power. However, as noted above and discussed infra, the question is not, as Ameritech alleges, whether the states have the authority to regulate interstate services, but rather, whether the states have the authority to regulate inseverable, jurisdictionally mixed services absent federal preemption. Contrary to Ameritech's claims, state commissions possess precisely this authority.

10 The ILECs also argue that this authority is beyond that of the state commissions; yet, as discussed infra, they ignore the Act's preservation of state authority under Sections 251(d)(3) and 261(c).

not require the ILECs to incorporate non-enumerated terms regarding interstate services.[11] Surely, Congress could not have intended to empower the FCC to leave the issue to the states, but not empower it to promulgate rules to guide the states in their exercise of that authority.[12] The ILECs' attempts to torture the plain language of the statute by reference to earlier sections should be rejected.

B. State Commission Authority Under Federal Law

To the extent that the Commission determines that it is appropriate to leave the regulation of inter-carrier compensation for the exchange of ISP-bound traffic entirely to the states, the Act preserves states' authority to impose such regulations. Section 251(d)(3) provides as follows:

> PRESERVATION OF STATE ACCESS REGULATIONS. -- In prescribing and enforcing regulations to implement the requirements of this section, the Commission shall not preclude the enforcement of any regulation, order, or policy of a State commission that (A) establishes access and interconnection obligations of local exchange carriers; (B) is consistent with the requirements of this section; and (C) does not substantially prevent implementation of the requirements of this section and the purposes of this part.[13]

State rules governing ISP-bound traffic meet each of these three requirements. The first prong of the test requires that the state policy establish "access and interconnection obligations." The phrase "access and interconnection" is not defined in the statute, but is used elsewhere in the

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[11] Indeed, such an interpretation would simply force the adoption of an empty formalism, whereby state regulators adopt federal rules as state requirements.

[12] SBC avers that the Act's legislative history "makes it plain that Congress never intended any interconnection-related provision of Section 251 to be used in furnishing any interexchange service." SBC Comments at 6. As discussed infra, the question is not whether interconnection agreements govern interexchange services, but rather whether these agreements can govern jurisdictionally mixed, inseverable services.

[13] 47 U.S.C. § 251(d)(3) (emphasis added).

Act to encompass all aspects of carrier interconnection necessary for competitive entry, and there is every reason to conclude that Congress intended a similar meaning in Section 251(d)(3).[14]

For example, Section 271(c)(1)(A) requires that a BOC, in order to meet so-called "Track A" of Section 271, demonstrate that it has entered into an approved interconnection agreement under which the BOC is providing "access and interconnection to its network facilities" to a competing LEC. The FCC has construed a request for "access and interconnection" under Section 271(c)(1)(A) to be a request that, if implemented, will lead to facilities-based competition.[15] It would make no sense to view such a request as necessarily including only interconnection under Section 251(c)(2) and access to unbundled network elements under Section 251(c)(3), as the ILECs urge the Commission to do, since potential competitors may need many other services (e.g., number portability, collocation, etc.) for successful entry.

This view is confirmed by the language of Section 271(c)(2)(B), the competitive checklist provision, which states that "[a]ccess and interconnection includes each of the following [14 items listed in the checklist]." Those 14 items encompass much more than interconnection under Section 251(c)(2) and access to network elements under Section 251(c)(3). For example, Section 271(c)(2)(B)(viii) of the checklist requires a BOC to provide "[w]hite pages directory listings for customers of the other carrier's telephone exchange service." This service is not required by

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14 Where the same words are used twice in the same act, there is a presumption that they have the same meaning. See Gustafson v. Alloyd Co., 115 S. Ct. 1061, 1067 (1995).

15 See Application by SBC Communications, Inc., Pursuant to Section 271 of the Communications Act, of 1934, as amended, To Provide In-region, InterLATA Services in Oklahoma, Memorandum Opinion and Order, 12 FCC Rcd 8685, ¶ 54 (1997), aff'd, SBC Communications, Inc. v. FCC, 138 F.3d 410 (D.C. Cir. 1998).

Section 251(c)(2) (interconnection) or Section 251(c)(3) (unbundled elements) or any other provision of Section 251.[16] Moreover, white pages listings are used for intrastate and interstate calls. Accordingly, the only reasonable and internally consistent reading of "access and interconnection" obligations is a broad one that encompasses matters of a jurisdictionally mixed nature and addresses issues both within and outside of those areas covered by Section 251's federal requirements. Given that the purpose of Section 251(d)(3) is similar to the purpose of the competitive checklist (both are intended to ensure the availability of adequate interconnection arrangements), it is logical that the terms of Section 271 should inform the meaning of Section 251(d)(3) and that the latter should be construed to cover all aspects of carrier interconnection.[17]

The second and third prongs of Section 251(d)(3)'s test are also easily met. Those requirements are that the state regulation, order or policy (1) be consistent with the requirements

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[16] Section 251(b)(3) requires all LECs to permit competing carriers "to have nondiscriminatory access to . . . directory listing." 47 U.S.C. § 251(b)(3). The FCC has construed this provision to require that a LEC permit its competitors' customers to obtain directory listings from the LEC's directory assistance on nondiscriminatory terms and conditions. See Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, Second Report and Order, 11 FCC Rcd 19392, ¶¶ 133-35 (1996). In contrast, Section 271(c)(2)(B)(viii) requires that a BOC allow its competitors' customers to be listed in the BOC's white pages. See Application by BellSouth Corp., BellSouth Telecommunications, Inc., and BellSouth Long Distance, Inc., for Provision of In-Region, InterLATA Services in Louisiana, Memorandum Opinion and Order, 13 FCC Rcd 20599, ¶¶ 253-259 (1998). The requirements are therefore different.

[17] A broad reading of "access and interconnection" is independently supported by Section 251(a)'s interconnection requirements. The Section 251(a) duty "to interconnect directly or indirectly with the facilities and equipment of other telecommunications carriers," 47 U.S.C. § 251(a), would be subverted if an incumbent LEC refused to pay for the exchange of traffic. To ensure compliance with Section 251(a), therefore, a state may, under Section 251(d)(3), require that carriers be fairly compensated for the exchange of traffic between networks.

of Section 251, and (2) not substantially prevent implementation of Section 251 or Part II. The FCC has expressly ruled that "[a] state commission's decision to impose reciprocal compensation obligations in an arbitration proceeding -- or a subsequent state commission decision that those obligations encompass ISP-bound traffic -- does not conflict with any [FCC] rule regarding ISP-bound traffic."[18] There is no question therefore that states may, pursuant to Section 251(d)(3), exercise authority over all contractual and regulatory issues relating to the exchange of ISP-bound traffic.

Other provisions of the Act also provide states authority to prescribe rules governing inter-carrier compensation rates. Section 261(c) preserves for states the authority to prescribe requirements in addition to those prescribed pursuant to Sections 251-252 when necessary to further competition in the provision of exchange or exchange access service:

> ADDITIONAL STATE REQUIREMENTS. -- Nothing in this part precludes a State from imposing requirements on a telecommunications carrier for intrastate services that are necessary to further competition in the provision of telephone exchange service or exchange access, as long as the State's requirements are not inconsistent with this part or the [FCC's] regulations to implement this part.[19]

Thus, Section 261 preserves for states the authority to apply state law within the context of a state's review or enforcement of interconnection agreements or in generic state proceedings.[20]

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18 Implementation of the Local Competition Provisions in the Telecommunications Act, CC Dkt. No. 96-98, Declaratory Ruling, FCC 99-38, ¶ 26 (rel. Feb. 26, 1999).

19 47 U.S.C. § 261(c).

20 As recognized by a federal district court, "the Section 252 negotiation procedure is not the sole means for the [state commission] under the federal statutes to order and regulate telecommunications." Michigan Bell Tel. Co. v. Ameritech Mich., 26 F. Supp. 2d 993, 1000 (W.D. Mich. 1998). Sections 261(c) and 251(d)(3) preserve additional means. Id.

There can be no question that, under Section 261(c), states can apply state law to ensure that ISP-bound traffic is compensated at parity with Section 251(b)(5) traffic. First, such a result is "necessary to further competition in the provision of . . . exchange access."[21] Second, as the incumbent LECs have asserted, ISP-bound traffic is jurisdictionally mixed, and it is not feasible to separate the intrastate from the interstate components.[22] Thus, a state cannot ensure viable interconnection arrangements between carriers for the exchange of intrastate traffic without applying its decision to the interstate ISP-bound traffic.

There is also no basis for concluding that a state may only apply state law under Section 261(c) to purely intrastate services and not to jurisdictionally mixed services. Section 261(c) contains no such limitation. On the contrary, it permits a state to apply state law to intrastate services whenever necessary to further exchange and exchange access competition and so long as doing so would not undermine the provisions of Part II and the FCC implementing regulations. Section 261(c) therefore empowers states to fill the interstices in the federal local competition regime established under the Act. It would be strange indeed to conclude that Congress did not

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21 See 47 U.S.C. § 261(c). The application of reciprocal compensation to the exchange of ISP-bound traffic easily meets the requirement that it be "necessary to further competition." This is because competition will be stifled if carriers cannot interconnect and exchange traffic in accordance with their negotiated agreements, and, more importantly, on just and reasonable terms and conditions.

22 See, e.g., BellSouth Comments at 11; GTE Comments at 17-18; SBC Comments at 27.

want the states to perform this function for any intrastate service that was "contaminated" by even the most minimal interstate component.[23]

Finally, the application of state law in this manner is fully consistent with Part II of Title II and the FCC's regulations. This analysis is similar to the second and third prongs of the Section 251(d)(3) analysis discussed supra. Thus, Section 261(c) permits states to exercise jurisdiction over the contractual and regulatory issues related to the exchange of ISP-bound traffic.

C. State Commission Authority Under State Law

Finally, the ILECs, in particular Ameritech, contend that, even assuming arguendo that the Commission could lawfully allow the states to regulate interstate traffic,[24] state commissions generally lack the authority to do so. First and foremost, the question is not whether state commissions have the authority to regulate interstate services; the question is whether state commissions have the authority to regulate inseverably jurisdictionally mixed services in an area not preempted by the FCC. The answer to that question is unequivocally yes. To the extent that local ISP-bound traffic is inseverably mixed with interstate traffic, Section 2(b) fully preserves a state's ability to establish inter-carrier compensation arrangements for all ISP-bound traffic unless and until preempted by the FCC.

Section 2(b) provides that, with certain exceptions not relevant to this analysis:

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23 In any event, even if one ignores the underlying context and purpose of Section 261(c), the discussion of Section 2(b) infra demonstrates that a preservation of state authority over intrastate services permits the state to regulate jurisdictionally mixed services.

24 As noted, the Eighth Circuit has upheld the FCC's authority to allow state regulators to set rates for the recovery of interstate costs related to ISP-bound traffic. See Southwestern Bell, 153 F.3d at 541-43.

> [N]othing in this Act shall be construed to apply or to give the Commission jurisdiction with respect to . . . charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communications service by wire or radio of any carrier. . . .[25]

As the Supreme Court observed, in its landmark Louisiana PSC opinion, Section 2(b) is extremely broad. It addresses the "appropriate division between federal and state regulatory power" with respect to all "charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communications service. . . ." Louisiana Pub. Serv. Comm'n v. FCC, 476 U.S. 355, 372-73 (1986) (emphasis added). Indeed, the Louisiana PSC Court sharply rejected arguments that Section 2(b) acts to preserve state jurisdiction to regulate "only when two factors are present; first, when the matter to be regulated is purely local and second, when interstate communication is not affected by the state regulation which the FCC would seek to preempt." Id. at 373-74 (emphasis added). Instead, the Court held that the Section 2(b) standard focuses on whether state regulation would "negate" or otherwise "thwart or impede" the lawful exercise of federal authority, as reflected in the Communications Act and FCC rules and policies adopted pursuant thereto.[26]

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[25] 47 U.S.C. § 152(b)(1). Obviously, if the Commission concludes, as it should, that states have authority to regulate rates for the exchange of ISP-bound traffic under Sections 251-252 and 261(c), then it need not reach Section 2(b).

[26] See, e.g., Louisiana PSC, 476 U.S. at 375 n.4; National Ass'n of Regulatory Util. Comm'rs v. FCC, 880 F.2d 422, 429-30 (D.C. Cir. 1989) ("NARUC III"). As Justice Scalia's majority opinion in Iowa Utilities Board indicates, after the 1996 Act, Section 2(b) "may have less practical effect," because "Congress, by extending the Communications Act into local competition, has removed a significant area from the states' exclusive control." AT&T v. Iowa Utils. Bd., 119 S. Ct. 721, 731 n.8 (1999). However, at least in those instances where the 1996 Act's local competition provisions are "silent" (as we have assumed, in this section of our analysis), Justice Scalia acknowledges that "[Section 2(b)] continues to function." Id.

Since Section 2(b) was adopted, states have on numerous occasions been permitted to regulate "mixed-use" facilities and services employed in connection with intrastate and interstate communications, in a wide range of contexts, in the absence of a conflicting federal rule. For example, in its 1977 NCUC II decision affirming the FCC's establishment of its Part 68 terminal equipment registration program, the U.S. Court of Appeals for the Fourth Circuit observed that "the vast majority of terminal equipment has been -- and is -- regulated by the states," although "the FCC has never conceded that joint equipment [i.e., equipment employed in connection with intrastate and interstate services] is beyond federal jurisdiction, should the need for federal action arise."[27] While confirming its earlier determination in NCUC I that interconnection rules adopted by the FCC must preempt any contrary state regulations, the Court noted that "federal primacy in regulation of jointly used terminal equipment" did not, as a jurisdictional matter, curtail state ratemaking prerogatives.[28] Several years later, in its Computer II Reconsideration Order, although it preempted state regulation that conflicted with its new Computer II unbundling and detariffing policies, the Commission made clear that its decision did not foreclose "future attempts by the states to regulate CPE in ways which they perceive to be consistent with this decision."[29]

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27 North Carolina Utils. Comm'n v. FCC, 552 F.2d 1036, 1050 (4th Cir. 1977) (emphasis added) ("NCUC II").

28 Id. at 1048.

29 See Amendment of Section 64.702 of the Commission's Rules and Regulations, Memorandum Opinion and Order, 84 FCC 2d 50, ¶ 154 (1980); see also Filing and Review of Open Network Architecture Plans, Memorandum Opinion and Order, 4 FCC Rcd 1, ¶ 85 n.156, ¶ 277 (1988) (FCC declined to require that certain LEC-provided services, such as call forwarding and call waiting, be federally tariffed); Illinois Bell Tel. Co. v. FCC, 883 F.2d 104, 114 (D.C. Cir. 1989) (same, Centrex services); MTS and

As these examples demonstrate, Section 2(b) permits a state commission to regulate, pursuant to its authority under applicable state law,[30] jurisdictionally mixed facilities and services. In such cases, rules and policies adopted by the state commission in the exercise of its own jurisdiction will stand unless and until they are found to "negate" or otherwise "thwart or impede" the lawful exercise of federal authority under the Communications Act or applicable FCC rules and policies.

III. THE ILEC PROPOSALS RELATING TO REVENUE SHARING AND MEET POINT BILLING SCHEMES ARE BASED UPON FAULTY ASSUMPTIONS AND A MISUNDERSTANDING OF THE COSTS INCURRED BY THE CLECS IN TRANSPORTING AND TERMINATING ISP-BOUND TRAFFIC.

A. The ILECs' Assertions That They Do Not Fully Recover Their Costs On ISP-Bound Calls Are Based Upon Faulty And Unsupported Studies.

As expected, the initial comments of several ILECs attempt to portray a variety of economic harms due to the payment of compensation to CLECs for completing calls to ISPs. The ILECs claim either that they themselves are damaged, or that compensation for ISP-bound traffic creates economic disincentives for competition or efficient network utilization. These allegations do not withstand even minimal scrutiny. Instead, the ILECs' assertions actually provide additional economic support for continuing current inter-carrier payments for ISP-bound traffic.

WATS Market Structure, Decision and Order, 4 FCC Rcd 5660 (1989) (states allowed to regulate charges for certain mixed-use special access lines).

30 While Ameritech may be correct that state commissions lack authority to regulate purely interstate matters, state commissions typically have express authority to regulate the inseverably intrastate portion of a jurisdictionally mixed service, and, by extension, the inseverably interstate portion, unless preempted by the FCC.

Most ILECs' claims in their initial comments of economic harms are essentially undocumented and conclusory. Only Ameritech attempted to quantify the losses it claims to incur when it provides a second access line for Internet traffic that is sent to a CLEC.[31] Applying average Internet usage data and state-specific cost and revenue figures, Ameritech purports to show that its second access line market for Internet users is a money-losing proposition in each of its five states, irrespective of whether the state prices local calls on a usage sensitive basis.

However, Ameritech's simple analysis contains at least three significant errors. Two of the errors uncovered in the Ameritech study are internal to the study itself. First, Ameritech fails to recognize the lower incremental costs of second lines. Second, Ameritech fails to reflect the sharing of transport costs between ILECs and CLECs in most interconnection agreements. Equally important, Ameritech also fails to consider its long run cost savings -- specific to high volume Internet access -- that are due to CLEC activities, growth, and new technologies. When these errors are corrected (without changing any of Ameritech's usage or revenue inputs) the second access line market analyzed in the study produces substantial net revenues and cost savings in four out of five Ameritech states.[32]

First, the analysis attributes, as the cost of a second access line, the same cost used to set the rate for a single unbundled loop -- which is then adjusted for retailing costs. It is not correct to attribute the unbundled element cost in this manner. The single line costs include, and recover,

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31 Ameritech Comments, Attachment A, "Cost vs. Revenue Analysis for a LEC Providing Service to an End User of an ISP Served by Another LEC."

32 Only in Wisconsin is the second access line market a money loser. However, as discussed infra, state specific conditions in one of Ameritech's states cannot be used to justify a failure to compensate CLECs for transporting and terminating ISP-bound traffic.

costs that are saved when a second or even third access line is provisioned for a customer. These costs include the network interface device (NID), the structure and placement costs for multiple distribution lines, and part of the distribution plant itself. Publicly available UNE cost models such as the HAI model show that these costs range between 45% and 67% of the total costs of the UNE line.

The most efficient provisioning method for subscriber lines involves incurring these costs once, well before demand for second or third lines may develop. By the same token, the costs are recovered from the time the first line is placed in service. Any other method would involve a necessarily imprecise forecast of additional access line penetration and require that the unit costs of all access lines be recalculated frequently as the demand actually materialized. The effects of this cost allocation to primary lines are well recognized in the industry. In fact, several ILECs such as U S West have submitted second-line TELRIC or TSLRIC cost studies to state commissions demonstrating that these access lines are less costly to turn-up and hence more profitable that first access lines.

Accounting for Ameritech's failure to recognize NID and distribution plant-related savings eliminates between 56% (Illinois) and all -- 103% for Indiana -- of the estimated deficit associated with second access lines (except in Wisconsin). In accounting for this cost reduction, we assumed the second line cost savings associated with NIDs and distribution plant already placed to serve the first access line were <u>below</u> even the lower bound of the range developed in the HAI model for different density zones. The analysis is therefore quite conservative and, of course, specifying a higher percentage of loop plant that was already in place would eliminate more of Ameritech's alleged revenue deficiency.

Second, Ameritech's analysis attributes all of the tandem and direct transport costs associated with Internet traffic over the second access line solely to the ILEC. But interconnection agreements almost universally require that transport costs be split 50-50 between the ILEC and the CLEC where the ILEC's transport facilities are used to carry traffic all the way to the CLEC's location.[33] Ameritech's failure to account for a 50-50 split is exacerbated by the traffic volume used in the analysis for Internet calls -- about one hour and 20 minutes per day per user.[34] Accounting for the CLECs' share of the transport costs used in the Ameritech study eliminates between 17% and 19% of the estimated second access line deficit (except in Wisconsin).

Finally, the Ameritech analysis ignores the cost savings that the company realizes if the Internet calls are handed off to a CLEC, rather than requiring Ameritech itself to complete the call. These savings would not be realized by an ILEC in an environment of absolute monopoly[35] because the cost avoidance is directly attributable to the presence of CLECs handling ISP calls. Absent an ILEC obligation to provide inter-carrier compensation to CLECs, these cost avoidances would enhance the ILEC's bottom line in the same way that added revenues generated

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33 The 50-50 split in the interconnection agreements is a surrogate for a more precise type of meet-point arrangement, for which the added calculation costs would not be warranted by the low economic costs of transport using current network technologies.

34 In comparison, the average time spent online by AOL's subscribers, of which there are over 17 million, is 55 minutes per day. See "AOL Tops 17 Million Subscribers, is Target of Labor Complaint," Vol. 19, No. 72 Comm. Daily at 7 (Apr. 15, 1999). For a 30 day month, the total is 27½ hours online. Ameritech's estimate of 39 hours is 40% higher than AOL's average subscriber's usage.

35 See Global NAPS Comments, Exhibit 1, Statement of Fred Goldstein ¶ 10 ("Goldstein Statement").

by second access lines or shared transport costs would. Part of the cost savings is also due to new technologies available to all LECs. Contrary to the ILECs' claims, if inter-carrier compensation for Internet traffic discriminated among different types of access technologies, it would distort CLECs' incentives to adopt the most efficient technologies -- technologies that could increase the incumbents' cost savings over time. Thus, in order to obtain an accurate picture of Ameritech's long run costs, these savings must be included. Otherwise, originating ILECs will realize windfall gains.

The ILEC's cost savings can be calculated in several ways. One way is to assume that if it did not hand off the calls to CLECs, an ILEC would terminate the call to an ISP using a mixture of ordinary end office switching, and lower cost data network offload technologies. The data network offload solution requires high volumes of traffic; at some locations the ILEC would simply switch the Internet call to the ISP. We assumed that, in the absence of a CLEC willing to handle the traffic, the ILEC would use a 50-50 mixture of end office switching and data switching.[36] At this ratio, between 50% and 100% of the second access line deficiency claimed by the Ameritech study is offset by the CLEC's participation in handling the traffic (except Wisconsin).

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[36] The estimated cost of data switching outside the circuit switched network was taken from the Telcordia (Bellcore) paper that ALTS discussed in Attachment A to its opening comments. The data cost is based on a DS3 port at 80% fill and adding back Ameritech's retail costs. James Gordon and Amir Atai, "Economics of Internet Offload and Voice/Data Integration," Bellcore TM-25927, Issue 1, December 1998, at p. 3.

Alternatively, one might use the lower end of the cost range estimated for ILEC network upgrades needed to handle Internet calls over the next five years.[37] These are costs that ILECs might incur in the absence of exogenous influences such as growing competition from CLECs and faster deployment of alternative data access technologies like xDSL. This alternative assumption amounts to an estimate of ILEC costs if they maintained a monopoly -- at least with respect to Internet calls. That is, these are the costs ILECs might incur in order to both terminate Internet calls to ISPs and carry Internet calls originated by the its subscribers. The savings ILECs realize by foregoing a monopoly over Internet calls offset between 36% and 82% (except in Wisconsin) of the entire state-specific deficit from second access lines shown in the Ameritech study.

All together, these three modifications to Ameritech's study offset well over 100% of its claimed deficiency from serving second access lines used to originate calls to ISPs via CLEC networks. These results apply in four states, and, contrary to Ameritech's analysis, are entirely confirmed by Ameritech's and other ILECs' continuing strong economic performance.[38] The only

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37 The low end ILEC impact estimated by the Gordon/Atai paper cited in the previous footnote amounts to about $2.65 per month per line for the model ILEC used in the paper. Note that ALTS demonstrated in its initial comments that most or all of the possible ILEC future costs could be avoided based on the development of new technologies like xDSL and cable modems.

38 For example, on April 20, 1999, the newswires contained this report (excerpted). Baby Bells Meet Forecasts . . . New York (Reuters) - First quarter profits at three regional local phone companies were in line with Wall Street expectations . . . Results at local phone companies BellSouth Corp. and merger partners SBC Communications Inc. and Ameritech Corp. were driven by strong demand for data services, phone features such as Caller ID, and extra phone lines for fax machines or Internet access. Shares of Ameritech increased $1.06 to $63.19, while SBC gained 75 cents to $53.69. BellSouth was unchanged at $41.875 . . . BellSouth's first quarter profit fell 31 percent because of foreign currency losses and higher capital spending but the Atlanta-based local phone company's results still slightly exceeded Wall Street expectations . . . BellSouth's revenues

state in which an apparent deficiency continues to exist is Wisconsin. However, the monthly residential service rate in Wisconsin is only $5.75, or about $6.80 per month (55%) lower than the residence rate set for Ameritech in Indiana -- a state with demographic and telephone network characteristics similar to Wisconsin.[39] At the same time, the offset in Indiana is greater than 200%. Thus, any differences in net effects in Indiana or Wisconsin (as well as Ameritech's other three states) are entirely attributable to intrastate pricing differences, constitute state-specific conditions, and lend no support to the view that this Commission's interstate inter-carrier compensation should be colored by the Ameritech study. As ALTS has argued before, if there is a problem in a state where local rates do not cover the ILEC's costs, the ILEC should seek a solution within its intrastate rates and rate structure.

B. Even If The ILECs Are Not Fully Recovering Their Costs, The Solution Is Not To Make The CLECs Share In Any Purported ILEC Shortfall.

While Ameritech was the only ILEC that attempted to quantify the money losing effects of Internet calls, the other ILECs put forth several economic arguments against continuing inter-carrier compensation for Internet calls, all of which are also rooted in the premise that such calls lose money for incumbents. Next, the ILECs attempt to convince the Commission that, not only

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increased 10.1 percent to $5.97 billion, up from $5.43 billion a year ago. SBC's profits increased to $1.1 billion or 56 cents a share, compared with profits of $985 million or 50 cents a year ago. SBC's results met Wall Street's forecasts, according to First Call Corp . . . Ameritech earned $732 million or 66 cents a share in the first quarter, compared with last year's $492 million or 44 cents. Excluding one-time items, Ameritech's profits increased 19.5 percent to $705 million or 63 cents a share, compared with earnings of $590 million or 53 cents a share a year ago.

[39] The Wisconsin rate is also well below the comparable rates in Michigan and Ohio, and would be below Ameritech's combination of fixed and usage sensitive residence revenues in areas of Illinois outside of Chicago.

should it not require them to compensate the CLECs, but indeed, that the CLECs should really be ordered to compensate the ILECs. Again, the notion that the incumbents lose money on subscriber calls to ISPs underlies the ILECs proposals' to extract more revenues from the CLECs, ISPs, or both -- in the form of "revenue sharing," applying "Feature Group A" pricing to Internet calls or assessing the so-called "special access surcharge" of $25.00 per month per voice grade equivalent line.[40]

1. ILECs' Qualitative Economic Arguments

SBC's initial comments perhaps best summarize the ILECs' claims of economic harm from inter-carrier compensation for Internet calls.[41] SBC sets forth four types of alleged economic distortions, which it does not attempt to quantify.[42] SBC argues that payment will (1) retard local competition because CLECs will be unwilling to serve local end users who are ISP subscribers; (2) result in inefficient market entry; (3) result in irrational pricing schemes; and (4) impede the deployment of new data technologies. As to the idea that inter-carrier compensation

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40 SBC's initial comments provide a lengthy recitation of the special access surcharge. SBC Comments at 23 & n.45. SBC's analysis overlooks two important points, however. First, the switched access charges for which the surcharge was first established as a surrogate in 1983-84 have declined by 75% to 80% since then. The special access surcharge is thus grossly out of line with the current prices it was supposed to emulate. Second, as a result of this distortion, application of the $25.00 per month surcharge per voice grade line to either CLECs or ultimately to the ISPs would grossly distort the costs of ISDN PRI, DS3 facilities or new technologies like xDSL that ISPs must use in order to efficiently serve their growing numbers of customers.

41 SBC Comments at 18-19. We use SBC's qualitative arguments against inter-carrier compensation to address the like arguments made by other ILECs.

42 SBC's list of negative economic effects also illustrates the point made on page 16 of ALTS' initial comments, i.e., that the ILECs are arguing that it is both more costly and, at the same time, less costly for LECs to handle Internet calls.

will retard competition, SBC may have been too busy preparing its comments to notice the highly successful initial share offerings and superior share price performance of CLECs like Covad, Northpoint, Rhythms Netconnections and other providers whose business models explicitly focus on providing DSL services to residences. Perhaps SBC believes that it can continue to limit the development of these business strategies by its own effort to frustrate CLECs' collocation requirements and to limit access to data network UNEs like DSLAMS. On the other hand, Wall Street is perhaps the most efficient and well-informed competitive market of all. The Commission should rely on the signals that the capital markets are sending about providers who want to serve high volume residential ISP subscribers, and reject SBC's opposing claims.

SBC and other ILECs also claim that inter-carrier compensation for Internet calls would result in CLEC entry merely for the purpose of receiving windfall reciprocal compensation, and that Internet compensation will result in "irrational" pricing schemes where CLECs may actually pay ISPs. These points do not establish the kind of sustainable economic distortions that should eliminate the inter-carrier compensation. It may be that some CLECs have adopted niche market strategies focusing on ISPs and inter-carrier compensation. Such conditions, if they exist, have no bearing on public policy issues for two reasons.

First, such relatively narrow market strategies will be extremely limited in their overall economic effects. To be successful over the long run, CLECs must seek to serve as many different types of telecommunications customers, with different traffic patterns, in order to make use of their largely fixed costs of network capacity. A CLEC that focused only on terminating calls to ISPs would be dependent on a very narrow market segment. In addition, many other LECs, incumbents and competitors, are likely competing for this market segment as well. Even

the most well executed niche market strategy may not be successful. Second, by its very nature competition should beget a variety of different market strategies among different vendors, and public policies should not hamper such evolution. Only a monopolist would argue otherwise. Thus, ILECs' complaints that some CLECs may have adopted specialized strategies, including promotional arrangements for some ISPs, merely reflect the same ILEC efforts to try to push technology and competition back to the days of absolute monopoly.[43] Indeed, the ILECs' various pricing proposals for inter-carrier compensation all would result in just such a backward march.

Finally, SBC and other ILECs, at least implicitly, contend that inter-carrier compensation for Internet calls should be limited to circuit-switched access. For example, SBC's argument that CLEC compensation would create disincentives for deployment of new technologies -- an argument entirely contradicted by current market realities, in any event -- implies that ILECs view inter-carrier compensation for Internet traffic as being confined to older circuit-switch serving arrangements and excluding newer technologies. The implication, in other words, is that if the Internet calls were handled outside the traditional circuit switched network, then no compensation would apply. This view mimics the ILECs' efforts in CC Docket 98-147[44] and elsewhere to have the Commission draw new and unwarranted distinctions between "voice" and "data" calls, UNEs and network interconnection rules.[45]

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[43] See Global NAPS discussion infra n.46.

[44] Deployment of Wireline Services Offering Advanced Telecommunications Capability.

[45] Certainly, only a compensation regime that discriminated among Internet access arrangements based upon the types of technologies used to provide the access could possibly create such disincentives. If a local provider knew that selecting a more efficient new technology would choke off all compensation for its costs of providing Internet

The Commission has recognized in paragraph 29 of the NPRM that the carrier who completes the ISP call incurs a cost that would not be recovered but for the inter-carrier payment. As demonstrated earlier, it is also apparent that the interaction between the originating and terminating LECs provides distinct economic benefits to the incumbents, both in the form of increased profits and through cost savings.[46] Therefore, it follows that not only should current inter-carrier payments be continued, but that such payments for terminating Internet traffic should apply in some form to all current and future methods of accessing the ISP interconnection point. The same compensation should be paid for terminating Internet calls whether the terminating LEC uses traditional end office circuit switching, DSL systems or any other technology that results in Internet calls being offloaded from the PTSN.

It is likely true that over time the substitution of alternative data switching and other offload mechanisms will reduce the current average costs of call terminations. At this juncture, however, there is no need to depart from the state-approved rates for the identical local service

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access, it would at least have to carefully assess all the other effects of the technology change with heightened care. Any pricing regime that required the carrier to make artificial choices among technological options would involve serious economic distortions.

[46] The comments submitted by Global NAPS, Inc. explain in detail why CLECs have been especially capable of developing networks that are designed to handle ISP-bound traffic:

> While CLECs typically provide lower prices to the ISPs, CLECs actually bring a fundamentally different value proposition that is far more compelling than price alone. This can be summarized in one simple notion: CLECs actually like doing business with ISPs, and treat them as valued *customers*. ILECs for the most part only begrudgingly do business with ISPs, and when they do, they attempt to fit them into *ratepayer* models designed for an earlier era.

Goldstein Statement ¶ 5 (emphasis in original).

call terminations subject to reciprocal compensation. ALTS noted in its initial comments that cost studies produce per minute call termination costs of between 0.24 and 0.64, and that the range of these estimates is narrowed when the cost models are applied with the same inputs and assumptions. Existing reciprocal compensation rates generally fall within this range and these prices should be used to set the initial inter-carrier compensation for Internet calls. The effects of the substitution of new data switching technologies will be gradual and will involve significant initial investments by LECs as well as other getting started costs. Once these costs have been identified and amortized the current reciprocal compensation prices may well be reduced to reflect the new cost savings.

Until it is appropriate to develop new cost studies that fairly reflect the widespread use of the new technologies, the current cost studies will remain accurate and useful. These inter-carrier compensation arrangements will properly compensate the terminating LECs for the costs they incur today and reflect the real cost savings that CLECs in particular offer to ILECs by virtue of assuming the role of terminating Internet calls to ISPs. Equally important, this interstate pricing regime will not cause any ILEC to lose money on calls originated to the Internet -- an effect, if it exists, that is solely a function of intrastate price levels.

2. ILECs' Pricing Proposals

The ILECs' comments, having purportedly demonstrated why they need not compensate CLECs for terminating ISP-bound traffic, attempt to turn the tables and use this proceeding to increase their compensation for originating Internet traffic. For example, several ILECs suggest that they should be allowed to impose "revenue sharing" arrangements on CLECs who serve ISPs. Alternately, they argue that the compensation should be based upon archaic pricing

structures like Feature Group A. Before addressing the specifics of the ILECs' arguments, it is important to point out a fundamental flaw in the ILECs' comments: the ILECs are incorrect that inter-carrier compensation for ISP-bound traffic causes them to experience revenue shortfalls. If the inter-carrier exchange rate is set close to the ILECs' costs for terminating traffic, the ILECs should be indifferent as to whether they incur those costs themselves or pay another LEC for incurring them. If there were a revenue shortfall, it would be caused by some flaw in the state rates paid by ISP subscribers.

Moreover, it would be arbitrary and capricious for the FCC to design inter-carrier compensation rules to fix any purported shortfall. A great deal of data traffic remains entirely on the ILECs' network (i.e., where the ISP is served by the ILEC), and changes in inter-carrier compensation rules would not address shortfalls caused by this traffic. Further, it is fairly clear that CLECs will stop serving ISPs if they cannot recover the costs of terminating traffic to them. The ILEC proposals for inter-carrier compensation would thus force ISPs back on the ILECs' networks. But of course the revenue shortfall (again, assuming there is one) would still exist because it is local rates that cause the shortfall.

BellSouth and U S West, among others, urge the Commission to prescribe "revenue sharing" arrangements with respect to ISP traffic, or to set the inter-carrier compensation for Internet calls within the access charge model of the early 1980s.[47] Revenue sharing arrangements hearken back to the days in which the larger incumbents could enforce meet-point billing and similar arrangements on their smaller brethren. The precise cost basis for, or the equity of, these

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[47] See, e.g., BellSouth Comments at 9; U S West Comments at 9-10.

arrangements was relatively unimportant, because all of the incumbents were absolute monopolies. Today, these monopoly arrangements are not appropriate for ISP related traffic.

First, the arrangements would not necessarily be cost based. Traditional revenue sharing arrangements among monopoly were not cost based and may have reflected uneven divisions of revenue with smaller LECs -- a factor that was relatively unimportant to the absolute monopolies. A compensation regime that reasonably reflects the TELRIC costs of ISP-bound traffic provides the price signal expects from a functioning competitive marketplace. Second, the ILECs contemplate revenue sharing arrangements that would only operate in one direction. ILECs would obtain a slice of CLECs' revenues from ISPs, but CLECs would not share in revenues and cost savings they help create for ILECs that originate calls to ISPs. Third, the ILECs' revenue sharing propositions would involve exchanges (at least by CLECs to ILECs) of competitively sensitive customer contracts, revenues and other information. Sharing such information may not have been harmful when two or more monopoly ILECs were involved, but it is unreasonable to expect the ILECs' smaller competitors to accede to such requirements in a competitive market.

It would also be inappropriate to impose a Feature Group A solution to ISP-bound traffic. Under such a regime, of course, the ILECs would bill CLECs -- but the CLECs would have no avenue to recover these fees because of the ESP/ISP exemption from such access charges. Feature Group A rates still significantly exceed long run economic costs on a per minute basis. Applied to Internet calls the cost/price disparity from applying access charges would be magnified several times over. Faced with such huge cost increases with no avenue for recovering the increases, CLECs might well rationally abandon the ISP market. If the Commission were to

adopt such a pricing scheme, the view that the ILEC efforts would lead to re-monopolization of Internet calls would likely become quite well grounded.[48]

The ILECs' efforts to have the Commission adopt some form of Feature Group A compensation based upon interstate access charges is inconsistent with the existing treatment of ISP-bound traffic, including the rate structures applicable to that traffic, and should be flatly rejected. Under the local rate structure adopted by the states, local carriers must recover the costs of carrying calls to seven digit numbers within the same local calling area from the end user that initiates those calls. Calls to ISPs are included among the calls that local rates are designed to cover. This is why the costs of carrying this traffic are generally allocated to the intrastate jurisdiction under the separations rules.

CLECs cannot recover these costs from ISPs. ILECs do not, and raising CLEC rates to do so would simply price them out of the market. Thus, where the CLEC performs transport and termination on behalf of the ILEC, the ILEC must pay the CLEC for that service. This avoids the windfall to the ILEC and allows the CLEC to cover its costs. The fact that meet point billing is used for Feature Group A in no way means that meet point billing should be used for the exchange of ISP-bound traffic.

None of the ILECs pricing proposals should be adopted. As demonstrated, ILECs can and are making money from residential customers who originate significant numbers of calls to the Internet, particularly if CLECs handle the other end of the call. This is true even in

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[48] See, e.g., Global NAPS Comments, Exhibit 2, Declaration of Lee Selwyn ¶ 19. Ironically, one might argue that the ILECs re-monopolization would represent cutting off their metaphorical noses to spite their faces, because re-monopolization would require ILECs to incur precisely the costs that they avoid when CLECs handle Internet calls.

jurisdictions where such originating calls are part of a flat-rated local service. Virtually all local rates are averaged across regions and classes of customers. It is expected that ILECs will make money on certain customers and lose money on others. The real question is whether an ILEC can earn a reasonable return on all customers in the aggregate. The Ameritech study does not address this issue (which is one in any case that must be addressed by the states). As noted, the way to correct any revenue deficiencies lies at the state not the federal level. Moreover, as demonstrated above, originating ILECs who send ISP calls to a CLEC realize real economic benefits from doing so. The CLECs reasonably should expect to share in those benefits up to the level of the average economic costs of terminating the traffic.

IV. THE COMMISSION SHOULD AFFIRM CARRIERS' RIGHTS TO OPT INTO EXISTING AGREEMENTS FOR THE TERM OF THE ORIGINAL AGREEMENT.

Ameritech erroneously argues that Section 252(i) does not permit requesting telecommunications carriers to MFN into contract provisions governing Section 251(b)(5) reciprocal compensation, let alone those governing the exchange of ISP-bound traffic. See Ameritech Comments at 22-27. In fact, the Commission is free to construe the ambiguous terms of Section 252(i) far more broadly than Ameritech suggests. Moreover, sound policy supports a broad reading of Section 252(i) that encompasses all of the provisions of LEC interconnection agreements, including those addressing reciprocal compensation and the exchange of ISP-bound traffic.

Section 252(i) grants requesting telecommunications carriers the right to opt into "any interconnection, service or network element" included in an approved interconnection agreement. 47 U.S.C. § 252(i). Ameritech asserts that neither Section 251(b)(5) reciprocal compensation

nor inter-carrier compensation for ISP-bound traffic constitutes "any interconnection, service, or network element" covered by Section 252(i). Ameritech Comments at 22. Contrary to Ameritech's claims, the term "interconnection" is used in analogous contexts throughout the statute to incorporate all aspects of local interconnection, including but not limited to, all of the services included in Section 251. Significantly, Section 251, which includes Section 251(b)(5)'s reciprocal compensation obligation, is generically entitled "Interconnection." As noted earlier, the Commission has previously construed "access and interconnection" under Section 271(c)(1)(A) to cover all aspects of facilities-based competition.[49] Indeed, the competitive checklist provision in Section 271 states that "access and interconnection" as required by Section 271 "includes" reciprocal compensation. See 47 U.S.C. § 271(c)(2)(B), (c)(2)(B)(xiii). Ameritech's attempts to limit the term "interconnection" to Section 251(c)(2)'s duty to physically link two networks is unavailing.[50]

Moreover, it is indisputable that the Commission may construe ambiguous statutory language in any manner that is reasonable.[51] It is entirely reasonable for the Commission to construe the term "interconnection" as used in Section 252(i) to permit CLECs to pick and

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49 See Application by SBC Communications, Inc., Pursuant to Section 271 of the Communications Act of 1934, as amended, To Provide In-Region, InterLATA Services in Oklahoma, Memorandum Opinion and Order, 12 FCC Rcd 8685, ¶ 54 (1997), aff'd, SBC Communications, Inc. v. FCC, 138 F.3d 410 (D.C. Cir. 1998).

50 Similarly, the term "service" is extremely broad and could easily encompass the transport and delivery of ISP-bound traffic on reasonable terms and conditions. For example, the transport and termination of ISP-bound traffic could reasonably be characterized as a "service" provided under an agreement.

51 See Iowa Utils. Bd. v. FCC, 119 S. Ct. at 738 (citing Chevron U.S.A. v. National Resources Defense Council, 467 U.S. 837, 842-43 (1984)).

choose rights to inter-carrier compensation provisions. After all, each of the ILECs have argued vehemently before the Eighth Circuit and elsewhere that a requesting carrier could opt into a final agreement -- including one whose terms govern the exchange of local and ISP-bound traffic – but only if the carrier adopted the agreement in its entirety.[52] Nowhere did the parties argue that Section 252(i) did not encompass reciprocal compensation or any other portion or terms of an agreement. Now that the Supreme Court has upheld the FCC's pick and choose interpretation of Section 252(i), there is no basis for permitting a requesting carrier to opt into provisions governing the exchange of traffic as part of an entire agreement, but not on a term-by-term basis. As the Commission has recognized and the ILECs have elsewhere conceded, Section 252(i) serves primarily to "ensur[e] that carriers obtain access to terms and elements on a nondiscriminatory basis."[53] Any attempt to prevent CLECs from exercising their rights to adopt inter-carrier compensation arrangements must be rejected.

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52 In the words of the ILECs, "section 252(i) establishes a straightforward nondiscrimination rule, under which an interconnector is free to step into the shoes of another carrier if it wishes to accept the deal that the other carrier has struck." Reply Br. For Petitioners Regional Bell Companies and GTE at 47, Iowa Utils. Bd. v. FCC, 120 F.3d 753 (8th Cir. 1997).

53 See Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, First Report and Order, 11 FCC Rcd 15499, ¶ 1316 (1996).

V. CONCLUSION

For the foregoing reasons, ALTS urges the Commission to adopt rules whereby negotiations are the method by which inter-carrier compensation for ISP-bound traffic is determined in the first instance together with the rules that control other Section 251(b)(5) traffic when carriers cannot otherwise agree.

Respectfully submitted

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CERTIFICATE OF SERVICE

I, Trisha McLean, do hereby certify that on this 27th day of April 1999, copies of the attached Reply Comments of the Association for Local Telecommunications Services were hand delivered to the following parties:

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